



0000121122

Law Offices

MARTINEZ & CURTIS, P.C.RECEIVED
AZ CORP COMMISSION

MAY 26 2 22 PM '98

2712 North Seventh Street

PHOENIX, ARIZONA 85006-1090

Michael A. Curtis
Jay M. Martinez
William P. Sullivan
Susan D. Goodwin
Jeffrey A. Katz
Larry K. Udall
Anja K. Wendel
Paul R. Michaud
Jeffrey D. Dollins

Telephone (602) 248-0372
Telecopier (602) 266-8290

OF COUNSEL

Joseph F. Abate
Thomas Hine
G. Eugene Neil

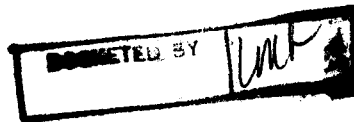
REFER TO FILE NO. 109-29-15-2

May 22, 1998

~~Arizona Corporation Commission~~
DOCKETED

MAY 26 1998

Ray T. Williamson, Acting Director
Utilities Division
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007-2996



Re: Preliminary Comments on the Staff Position on Electric
Competition

Dear Mr. Williamson:

The following are initial comments of Navopache Electric Cooperative.

On May 19, 1998, the Staff of the Arizona Corporation Commission requested comments on its Statement of Position on Retail Electric Competition. This Memorandum provides comments on the Staff position as that position affects Navopache Electric Cooperative.

Stranded Cost Issues

The Staff position is that utilities which divest all generation assets (including purchased power contracts) will have the opportunity to recover 100 percent of unmitigated stranded costs. The Staff position does not indicate whether or how the Commission will determine that the revenues brought in by divestiture are the maximum amount consistent with prudent risk management. Under the Staff proposal, there is no incentive for utilities to maximize the revenues from divestiture and no Commission oversight of the process. There should be.

If the utility does not divest its generation assets but instead sets up a corporate affiliate to which those generation assets are transferred, the Staff position on

stranded costs recovery appears to be as follows: The utility must demonstrate that divestiture is not practical and not in the public interest. The Commission may then provide transition revenues to preserve the utility's financial integrity. Navopache applauds this effort and suggest such would help the Plains entity.

Navopache, as a distributor, could theoretically sell purchased power contracts to third parties at market prices. As a practical matter it may be difficult for distribution cooperatives like Navopache to complete a sale by January 1, 2000, especially if RUS creates hurdles. Therefore, Navopache would be more likely to go the route of requesting transition revenues to preserve their financial integrity. Navopache believes this process will benefit members.

The Staff policy defers to the future treatment of stranded cost recovery periods, rates and filing dates. Does the Staff intend to re-do the stranded cost hearings or to make use of the hearings as put forth in the draft order? It will be important for cooperatives.

Stranded costs associated with a large load contract are essentially to be absorbed by the distribution cooperative under the Staff position. How this accomplished by a cooperative is unclear. It seems to be in conflict with the financial integrity policy.

Affiliate Rules

Separate corporate affiliates for competitive and monopoly activities must be created with no cost sharing between affiliates. This is important for cooperatives. This could also introduce additional costs, such as hiring additional staff and renting more office space. The additional costs for a small utility like Navopache could be large in percentage terms.

Similarly, the proposed policy of no joint marketing programs (between the utility and its affiliates) could be more expensive. Cooperatives may need joint efforts.

The Staff indicates that utilities must offer the same terms and conditions to all competitors and customers as it offers to itself. Presumably this policy applies to monopoly services. The Staff policy should be clarified. If it applies to competitive services, we would have a problem unless the utilities could define classes of customers themselves.

Because of potentially higher cost of separate affiliates for small utilities the affiliate rule should apply only to APS and TEP. All utilities would be subject to the rule that nondiscriminatory access to and pricing of monopoly services be provided.

Implementation of Competition

The Staff position is to open the market to competition for large customers (1 MW or more, including aggregations of smaller customers to meet the 1

MW threshold) on January 1, 1999. All customers will have access to competitive services on January 1, 2001. This schedule has the advantage of delaying for one year some metering and related problems. Navopache concurs.

The Staff policy is targeting a rate decrease for retail customers who are unable to choose competitive service during the transition period. The transition period is undefined. It could mean until January 1, 2001. Presumably the Commission will have to make a finding of fair value to implement the rate decrease or else enter into rate settlements with each utility. The policy prejudices the Commission's review of Navopache's rates and possibly imperils Navopache's ability to meet financial ratios.

The Staff position also requires utilities to offer 0.005 percent of residential customers access to the competitive market starting July 1, 1999, increasing 0.005 percent every quarter through the transition period. Customers can sign up on a first come first served basis. The utilities must submit a phase-in proposal by March 31, 1999. This is do-able but as the Commission changes its policy it has required the utilities to duplicate their previous work in developing customer selection plans.

Metering and Billing

Metering can be competitively offered to customers having access to competitive services. The Staff is proposing several meter protocols and permitting competitive customers with an hourly load under 20 kW to use load profiling after the transition period. With regard to billing, bills may be consolidated or provided separately by monopoly and competitive suppliers. Only the utility can order connects, reconnects and disconnects. There do not seem to be problematic provisions in this portion of the Staff proposal. However, there has to be a mechanism to develop the meter protocols.

Local Distribution Company Services

Cooperatives are unique. Utilities will provide standard offer service at regulated rates and collect a system benefits charge. No termination date for providing standard offer service is discussed. Does the Staff intend to change the current rule regarding termination of a requirement to provide standard offer service? Clarification is needed.

After the (undefined) transition period, power purchased to serve standard offer customers will be acquired through competitive bid. For Navopache, this means that they may not obtain the generation for the standard offer service from Plains. This essentially abrogates the Navopache-Plains all-requirements contract as it now stands, leaving only stranded costs to be recovered. Navopache commends this solution to the all-requirements contract dilemma presented to it by Plains Electric. Members should not be penalized for the non-competitive costs of essentially federally financed generation and transmission experiments which were intended to lower and not raise prices.

Transmission and Dispatch

The Staff's position is that utilities must provide non-discriminatory open access to transmission and distribution facilities to serve all customers. Such a policy is necessary for competition to work.

The Staff further requires utilities to join an independent system operator. Prior to the creation of an independent system operator, utilities must participate in an independent scheduling administrator. It is not clear whether the Commission has the authority to make such requirements. Further, independent system operators may not work out in other areas and requiring participation in an independent system operator may be premature. More discussion is needed on the roles of the independent system operator and administrator.

The Staff position is that the Commission will determine which generation units are must-run units for distribution reliability and mitigation of market power and will regulate the price of power from such units. There are several problems with this policy:

- The term "must run" needs to be defined. We think the Staff means units necessary to maintain voltage stability and similar aspects of reliability.
- Regulation of the price of power from must run units presupposes that only distribution utilities can provide the desired services. Why can't other companies provide such services in a competitive market?
- How will the Commission separate the power output from a must run unit into system reliability kW or kWh during a given period and generation for consumers during that period?
- If must run units also provide ancillary services for the transmission system, does the Commission have authority over the pricing of the services?

If the Commission desires to ensure system reliability why not require the utilities to submit plans for reliability and review those plans for adequacy. The utilities may purchase reliability-related services competitively, as necessary, as part of the plan.

With regard to the role of Navopache in the reliability business, Navopache and others may wish to purchase local generation (that does not now exist) to improve reliability in their distribution service areas.

The Staff proposal also indicates that costs of establishing and operating the independent scheduling administrator are recoverable from competitive customers. What about standard offer customers? It appears that all customers will benefit from or at least use the services of the independent system administrator. If most customers take service under the standard offer, recovery of costs only from competitive customers will make competitive power purchases very expensive and give standard offer customers a free trade.

Ray T. Williamson

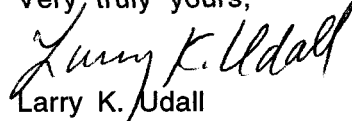
5/22/98

Page 5

The Staff position on transmission and dispatch seems to require major rethinking. It ought not to go forward as is.

Generally the Staff comments are progressive. Navopache would like to have further discussions.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Larry K. Udall".

Larry K. Udall

Counsel to Navopache Electric Cooperative

cc: Navopache Electric Cooperative